

TITLE 25. DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT

NOTICE OF PROPOSED RULEMAKING FOR THE UNIFORM MULTIFAMILY REGULATIONS, MULTIFAMILY HOUSING PROGRAM (MHP), JOE SERNA JUNIOR FARMWORKER HOUSING GRANT PROGRAM (JSJFWHG) AND HOME INVESTMENT PARTNERSHIPS (HOME) PROGRAM

Notice is hereby given that the Department of Housing and Community Development (Department) proposes to: (1) adopt new regulations creating uniform rules for multifamily rental housing assisted under the Multifamily Housing Program (MHP), Joe Serna Junior Farmworker Housing Grant Program (JSJFWHG) and HOME Investment Partnerships (HOME) Program; (2) amend the existing regulations for these programs to adopt the uniform rules; and (3) make other revisions to MHP. The purpose of the three effected programs is to provide financial assistance for affordable housing.

The text of the proposed regulations and regulation amendments, along with related documents, is available on the Department's web site (www.hcd.ca.gov).

WRITTEN COMMENT PERIOD

Any interested person, or his or her authorized representative, may submit written comments relevant to the proposed regulatory action by the Department. The written comment period begins May 9, 2003 and closes at 5:00 p.m. on June 23, 2003. The Department will consider comments received during this timeframe. Please address your comments to Michael Pope at mpope@hcd.ca.gov or Russ Schmunk at rschmunk@hcd.ca.gov. Comments can also be sent via mail to Michael Pope, Department of Housing and Community Development, P.O. Box 952054, Sacramento, California 94252-2054, or via fax to (916) 445-0117, attention: Michael Pope.

PUBLIC HEARINGS

Public hearings will be held in Los Angeles on Wednesday, May 28, 2003 commencing at 10:00 a.m. in the Ronald Reagan State Building Auditorium, located at 300 South Spring Street; in San Francisco on Thursday, May 22, 2003 commencing at 10:00 a.m. at the Hiram Johnson State Building Auditorium, located at 455 Golden Gate Avenue; in San Diego, on Tuesday, May 27, 2003 commencing at 10:00 a.m. at the San Diego State Building, Room B-109; in Fresno on Monday, June 16 commencing at 1:00 p.m., at The Californian, 851 Van Ness, Ballroom; and the final hearing to be held in Sacramento at the Departments headquarters on Monday, June 23, 2003 commencing at 10:00 a.m. located at 1800 Third Street, Room 183/185. Any person may present statements or arguments orally or in writing relevant to the proposed action described in the Informative Digest below. The Department requests, but does not require, that persons who make oral comments at the hearing also submit a written copy of their testimonies at the hearings.

AUTHORITY AND REFERENCE

The Department is conducting this rulemaking activity under the authority provided by Health and Safety Code (H&S) Section 50406(n) and H&S Section 50675.1(c), and to implement, interpret, and make specific Sections 50517.5 – 50517.11, 50675, and 50896 of the Health and & Safety.

INFORMATIVE DIGEST

The Department operates three programs that provide assistance for the construction or rehabilitation of affordable multifamily rental housing developments – the Multifamily Housing Program (“MHP”), the Home Investment Partnerships (HOME) Program (“Home”) and the Joe Serna, Jr. Farmworker Housing Grant Program (“JSJFWHG”).

- MHP is a state-funded program that makes low-interest loans to non-profit and for-profit private developers as well as to local public agencies.
- HOME awards and disburses federal funds made available to the State pursuant to Title II of Public Law No. 101-625, 104 Stat. 4079, known as the Cranston-Gonzalez National Affordable Housing Act of 1990 as amended by the Housing and Community Development Housing Act of 1992, Public Law No. 102-550. As part of this program, the Department makes grants to eligible cities and counties and direct loans to private organizations that qualify as Community Housing Development Organizations (CHDOs).
- JSJFWHG makes grants to local public entities and nonprofit corporations, and is permitted to make loans to limited partnerships if the funds would be used in conjunction with low-income housing tax credits, for the development of housing for agricultural workers and their families.

Rental housing developments funded by these three programs often are indistinguishable from one another. However, they often are underwritten to slightly different standards and are subject to other differing rules on the same subject. This has created difficulties in loan underwriting and long-term monitoring for Department staff. This also has created difficulties for clients who must learn three different sets of underwriting and other rules.

A major purpose of these regulations is to adopt a uniform set of underwriting assumptions and other standardized rules for multifamily housing developments that will apply in all three programs (the “Uniform Multifamily Regulations”). In addition, the Department is making other changes to the MHP regulations. This rulemaking package has three major parts:

- ❑ The adoption of a new subchapter 19 in Chapter 7 of Title 25 of the California Code of Regulations that contains the Uniform Multifamily Regulations.
- ❑ Individualized amendments to each of MHP, HOME and JSJFWHG adopting the uniform standards.

- ❑ Amendments that are specific to the MHP, and are not related to the uniform standards.

Uniform Multifamily Regulations

Following is a summary of the uniform rules that are proposed to be adopted for all three programs:

Section 8300. Purpose and Scope - describes the purpose of Subchapter 19 and lists the authority for the three programs.

Section 8301. Definitions - adopts definitions applicable only to Subchapter 19.

Section 8302. Restrictions on Demolition - Establishes a uniform rule that projects involving demolition must replace the number of bedrooms demolished rather than the number of units demolished. This essentially is the current federal HOME rule.

Section 8303. Site Control Requirements - Establishes the operative requirements for site control at time of application. The proposed standard closely parallels current MHP and HOME requirements.

Section 8304. Unit standards - would prohibit differences between restricted and nonrestricted units in terms of size and amenities, similar to current MHP requirements.

Section 8305. Tenant selection - would establish fair and equitable tenant selection procedures, would prohibit local residency requirements and would establish the minimum number of occupants for a unit based on number of bedrooms, to prevent underutilization of units. The proposed rules closely parallel current MHP requirements.

Section 8306. Tenant Recertification - addresses the annual recertification requirements for income or occupancy status, particularly if a household's size changes.

Section 8307. Rental Agreement and Grievance Procedure - establishes the requirement for "just cause" evictions and the requirement for Department approval of the rental agreement. The proposed rules closely parallel current MHP requirements.

Section 8308. Operating Reserves - closely parallels current MHP regulations and establishes a minimum initial deposit of 4 months operating expenses, plus 4 months required replacement reserve deposits, plus 4 months on non-contingent debt service – all to be paid from development funding sources.

Section 8309. Replacement Reserves – closely parallels current MHP regulations and establishes, for new construction projects, a minimum initial annual deposit of 0.6% of estimated construction costs.

Section 8310. Underwriting Standards – in general, establishes the following underwriting assumptions: 5% project vacancy rate; 50% commercial space vacancy rate; operating expenses as specifically listed in the California Tax Credit Allocation

Committee (“TCAC”) regulations; first year debt-coverage-ratio of not less than 1.10:1 or greater than 1.2:1; and a requirement that the project show a positive cash flow for 15 years.

Section 8311. Limits on Development Costs (title changed to “Limits on Design Features”) – consistent with existing MHP and HOME regulations, requires that project development costs be reasonable compared to costs for other similar developments in the local area, establishes a limits on construction contractor profit and overhead and site development costs, and specifies that property acquisition costs shall not exceed appraised value.

Section 8312. Developer Fee for Tax Credit Projects – similar to current MHP regulations, allows total developer fee up to the level permitted by TCAC and limits developer fee paid from development funding sources based on a schedule tied to unit count and construction type.

Section 8313. Developer Fee for Non-Tax Credit Projects – limits developer fees to the per unit caps set forth above, without regard to the TCAC regulations, except in the case of HUD 811 or 202 projects. HUD 811 or 202 projects located in non-rural areas are limited to \$5,000/unit.

Section 8314. Use of Operating Cash Flow – this section establishes how to distribute the cash flow remaining after payment of operating expenses, debt service and reserve deposits. Basically, the order of payment would be: deferred developer fee, approved partnership and asset management fees, 50% to the borrower and 50% to HCD and other public lenders, in an amount proportionate to their loan, as a residual receipts payment on the HCD or public lender loan.

Section 8315. Subordination Policy – this section would establish HCD’s subordination policy to senior lenders and would clearly state the types of provisions HCD will not subordinate to including: a provision prohibiting HCD from exercising its remedies or requiring the senior lender’s consent to exercise its remedies; a provision eliminating HCD’s interest if a senior lender accepts a deed in lieu of foreclosure; a provision that permits the senior lender to modify its documents without HCD’s consent; or a provision that would require HCD to take on additional obligations, above and beyond those in its loan documents. The section also provides that HCD will not subordinate to a local government lender unless the local government loan is more than twice as much as the total HCD assistance to the development (including loans and grants).

Section 8316. Leasehold Security – this section establishes the minimum provisions that must be included in a lease for HCD to accept a lease as security in lieu of fee simple ownership. Basically, the section would require either that: (1) the lease be at least as long as the term of the Program loan or grant and the Program documents be recorded on the fee interest as well as the leasehold interest; or (2) the lease must have least 90 years remaining from the date the Program documents are recorded and the lease must not have certain specified provisions that weaken the Department’s security interest. Finally, where the lessee and lessor are related or affiliated parties, the Program documents must be recorded on both the fee and leasehold interest.

MHP-Specific Regulation Amendments

Following is a summary of the more substantive amendments specific to the Multifamily Housing Program:

Section 7301(g)(g) – deletes “single parent households” and “households enrolled in Welfare to Work programs” from the list of groups qualifying as “Special Needs Populations”.

Section 7301(ii) – specifies that income levels based on State Median Income are to be expressed in terms of Area Median Income.

Section 7311 – substantially revises the program’s rules related to tenant households whose incomes have risen to the point where they exceed the income limit applicable to their unit, mandating rent increases for some households (and filling vacant units with tenants meeting the original income qualification standard) and granting the sponsor discretion to increase rents for others.

Section 7312 (a) – allows sponsors to charge new tenants rents based on area median income, without regard to the cap required under 7312(c).

Section 7312(c) – revises the cap on annual rent increases from 150% of CPI to a flat 5%.

Section 7312(d) – grants the Department authority to approve rent increases above the amount allowed by the standard rent increase formula if required to preserve project fiscal integrity.

Section 7314 – adds specific cost reasonableness standards regarding site improvement costs.

Section 7320(b)(7) – adds a new application scoring criterion, to reflect the requirements of Health and Safety Code section 50675.13, which was added by SB 1227 of 2002. Under this new criterion, points will be awarded to projects that qualify as infill or adaptive reuse developments, or that are located in proximity to public transit, public schools, parks and recreational facilities, or job centers.

Section 7320(b)(5) – modifies the scale used to score application leveraging.

Section 7320(c) – adds a tiebreaker to the application selection process. The proposed tiebreaker is the average affordability of the restricted units.

IMPACT OF PROPOSED REGULATIONS

The regulations codify program requirements that will result in reducing the rent burden for low-income renter households in California by increasing and preserving the supply of affordable multifamily rental housing. The program helps alleviate the problems of large numbers of California’s renters facing excessive housing costs and overcrowded or substandard living conditions. Many of these lower-income renters also have special

housing needs arising from a disability. The program regulations are designed to provide financing to projects that meet the array of rental housing needs presented by these low-income and special needs populations.

AFFECT ON SMALL BUSINESS

The proposed regulations do not affect small businesses. The reason for this finding is that participation in the three effected programs is voluntary. Applicants to the program that qualify as small businesses have determined that program funds will provide the financing necessary to allow development of their projects. The non-profit and for-profit small business applicants benefit from the below market interest rate offered by the program.

LOCAL MANDATE

The proposed regulatory activity will not impose a mandate on local agencies or school districts. Eligibility for the program is limited to entities demonstrating willingness and capacity to develop affordable rental housing. In any case, participation in the program is voluntary.

FISCAL IMPACT

This regulatory activity does not impose any cost on any local agency or school district that is required to be reimbursed under Part 7 (commencing with sec. 17500) of Division 4 of the Government Code; neither does the regulatory activity result in any other nondiscretionary cost or savings imposed on local agencies or in any cost or savings to any state agency (other than the Department). Public entities, including local governments and nonprofits organizations are eligible to apply for loans from the programs effected by this rulemaking action. However, participation is voluntary, not mandatory.

By bringing the rules for various programs into conformance with each other, the Department believes that, over time, the proposed changes will result in modest reductions in administrative costs.

EFFECT ON HOUSING COSTS

By reducing the number of different sets of rules that project sponsors must comply with, these regulations will modestly reduce the costs of such compliance, which should modestly reduce the overall cost of housing assisted by the effected programs.

INITIAL DETERMINATION OF STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY EFFECTING BUSINESSES

The Department has made an initial determination that the proposed action will not have a significant statewide adverse economic impact directly effecting businesses, including the ability of California businesses to compete with businesses in other states.

ASSESSMENT STATEMENT

The Department has determined that the regulations will not significantly affect the creation or elimination of jobs in California; the creation of new businesses or the elimination of existing businesses within California; or the expansion of businesses currently operating in California. In any case, participation in the program would be voluntary.

STATEMENT OF POTENTIAL COSTS IMPACT ON PRIVATE PERSONS AND BUSINESS DIRECTLY AFFECTED

The Department is not aware of any cost impacts that a representative private person or business would necessarily incur in reasonable compliance with the proposed action. While private businesses (including nonprofits) and individuals are eligible to receive program funds under the program, participation is voluntary.

CONSIDERATION OF ALTERNATIVES

The Department of Housing and Community Development must determine that no reasonable alternative considered by the Department or that has otherwise been identified and brought to the attention of the Department would be more effective in carrying out the purpose for which the action is proposed or would be as effective and less burdensome to affected private persons than the proposed action.

AVAILABILITY OF TEXT OF PROPOSED REGULATIONS AND STATEMENT OF REASONS

The text of the proposed regulations, along with the Initial Statement of Reasons prepared by the Department, which provides the reasons for the proposals, is available on the Department's web site, at www.hcd.ca.gov. All information the Department is considering as a basis for this proposal is maintained in a rulemaking file, which is available for inspection at the address noted below. Copies can be obtained by contacting Michael Pope at the address and telephone number noted below.

AVAILABILITY OF CHANGED OR MODIFIED TEXT

Following the written comment period, the Department may adopt the proposed regulations substantially as described in this notice. If the Department makes modifications, which are sufficiently related to the originally proposed text, it will make the modified text--with changes clearly indicated--available to the public for at least 15 days before the Department adopts the regulations as revised. Please send requests for copies of any modified regulations to the attention of Michael Pope at the address indicated below. The Department will accept written comments on the modified regulations for 15 days after the date on which they are made available.

AVAILABILITY OF RULEMAKING DOCUMENTS

All of the information upon which the proposed regulations are based is contained in the rulemaking file, which is available for public review, by contacting the person named below.

AVAILABILITY OF FINAL STATEMENT OF REASONS

At the conclusion of this rulemaking, a Final Statement of Reasons will be prepared as required by Government Code section 11346.9. This document will be available from the contact person named below.

CONTACT INFORMATION PERSON

HCD: Michael Pope (916) 327-5704
or Russ Schmunk (916) 327-2867

HCD Back-Up: Lenora Frazier
(916) 324-3785

HCD Address: State Department of Housing and Community Development
1800 Third Street, Room 360
Sacramento, California 95814

HCD Website: Copies of the Notice of Proposed Action, the Initial Statement of Reasons, and the text of the regulations may be accessed through our website at www.hcd.ca.gov

HCD Facsimile No: (916) 445-0117

The Department invites interested persons to present statements or arguments with respect to alternatives to the proposed regulations during the written comment period. Direct inquiries concerning the substance of the proposed rulemaking action and any requests for the documents noted above should be made to either Michael Pope or Russ Schmunk at the following address:

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